PIPER & MARBURY

L.L.P.

1200 NINETEENTH STREET, N.W.

WASHINGTON, D.C. 20036-2430

202-861-3900

FAX: 202-223-2085

BALTIMORE
NEW YORK
PHILADELPHIA
LONDON
EASTON, MD

WRITER'S DIRECT NUMBER
(202) 861-6471
FAX: (202) 861-4160

August 19, 1996

<u>HAND DELIVER</u>

William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

      Re: Omnipoint Corporation
              WT Docket No. 96-59
              <u>*Ex Parte* Presentation</u>

Dear Mr. Caton:

        In conformity with section 1.1206(a) of the Commission's Rules, enclosed please find two copies of a written *ex parte* presentation for inclusion in the above-referenced docket. A copy of the attached presentation is also being delivered this day to Mr. Evan Kwerel of the Commission's Office of Plans and Policy and to Mr. Brett Tarnutzer of the Commission's Wireless Telecommunications Bureau.

        Should you have any questions concerning this matter, please contact the undersigned directly.
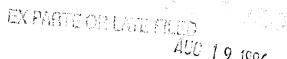
              Sincerely,

              Mark J. O'Connor
              Counsel for Omnipoint Corporation

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Enclosures

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Omnipoint Comments on FCC Procedures for the DEF-Block Auction

We applaud the efforts of the FCC to figure out ways to speed up the auction process, but we believe the current minimum bid increment matrix is too complex, has many inequities, and may well lengthen the auction process. Omnipoint strenuously urges the FCC to adjust the matrix so that the percentage increment is 5% at all levels of bidding activity and at any stage on a given market as in the prior auctions. This simplification ensures bidders can focus on responding to the demands of an auction that is already at least 3 times as complex as the C-block auction, due to the sheer number of licenses and the varying eligibility and financing for the different licenses.

A variety of unforeseen interactions and consequences otherwise may occur which result in more defaults and drag out the issuance of licenses, not shorten it. Should the FCC proceed, however, with a matrix whose percentages are graduated according to stage and bidding levels, we suggest this matrix be modified to address the following issues.

Issue #1: 15% increments (i.e., 32.2% minimally for the prior high bidder to respond) are too great a step and will sub-optimize the final outcome to all parties, including the government.

a. **Background:** When a market sustains three or more bids in a round, its minimum bid climbs by the greater of a fixed amount per MHz-pop and 15% in the following round. Thus, a "highly-contested" market (with as few as three bids) doubles in price based on 15% minimum increments every five rounds. This behavior is exaggerated in the D- and E-bands, where the current matrix uses the *sum* of bids in those bands.

b. **Problems:** On larger markets, this presents a situation where defending a high bid can cost tens of millions of dollars every other round. Such a pace eliminates much of the benefit of the multi-round auction where bidders are supposed to have a chance to learn the value that other bidders place on these large markets, and to weigh trade-offs among different bundles of markets at

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each step. Instead, the prices on these markets move in gigantic leaps, collapsing decision-making, and forcing premature contractions in eligibility.

Moreover, a high bidder on such a market must decide among (a) bidding back every other round at 32.2% jumps (i.e., a loss of a market followed by a re-bid, each at 15%, equals a two-round increase of 32.2%) to defend the market, (b) sacrificing the eligibility at stake on the market, or (c) seeking alternative markets simply to maintain its eligibility until the bidding increment declines, i.e., "parking." A high bidder may not bid back in defense, but rather contract eligibility simply because it could have afforded 10.3% more (i.e., a loss of a market followed by a re-bid, each at 5% equals a two-round increase of 10.3%) but not 32.2%. For example, under the existing matrix, in the case of a high bid on the New York BTA at $20/pop, the absolute increment to bid back this license totals roughly $120 million dollars for a single defense! **Such huge increments will leave money on the table from the perspective of the government**: when a bidder can justify another 5%, it may fall short of 15%; this ensures the government will sub-optimize its revenue from the auction, especially from the larger markets.

Parking on alternative markets to get around the "two-round look back effect" will cause a "reverse cascading" of bidding activity whereby bidders bid on smaller markets to maintain eligibility while they wait for the larger markets to have lower bid increments (this occurs for sure if many bidders wanting larger markets do the same thing). This tactic distorts outcomes in that smaller, more regionally-focused bidders will also be drawn into parking on otherwise "lightly-contested" or uncontested markets. It turns the natural waterfall effect of the simultaneous auction into a giant carom board. It upsets

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the natural assignment of value which proceeds first on "core" markets which logically should settle out before the surrounding smaller markets. Bidders interested in "core" markets who hold onto eligibility by bidding on smaller markets do so without knowledge of how "core" markets will settle out. In addition to lengthening the auction, it increases the risk that less sophisticated bidders overpay and become "stranded" on markets without owning the "cores." A likely outcome would be more defaults, more petitions to deny, and more reauctions.

c.   **Potential Solution:** If the FCC declines to make each cell be 5% in the minimum bid increment matrix, which we consider the best solution, we would alternatively recommend changing column C from 15% to 10% in each stage, and changing column B from 10% to 5% in each stage. The matrix would then look like:

		Column A: No New Bids in Most Recent Round	Column B: 1-2 New Bid in Pertinent Round	Column C: 3+ New Bids in Pertinent Round
Stage 1	% Increment: Absolute Increment:	5% $0.01 / MHz-Pop	5% $0.02 /MHz-Pop	10% $0.02 /MHz-Pop
Stage 2	% Increment: Absolute Increment:	5% $0.01 /MHz-Pop	5% $0.01 /MHz-Pop	10% $0.01 /MHz-Pop
Stage 3	% Increment: Absolute Increment:	5% $0.01 /MHz-Pop	5% $0.01 /MHz-Pop	10% $0.01 /MHz-Pop

Issue #2: Causing a license that is not even been bid on to suddenly go from a minimum increment of 5% to as much as 15% is not only arbitrary and unfair.

The current rules state that if **either** the D-band or the E-band is bid on, the other goes up in minimum increment percentage. This is particularly unfair since there are specific **technical** and partnering differences between the two bands. They have different numbers of microwave links in their respective spectrum and will require different guardband widths, depending on the choice of technology of the A- and B-band winners. Moreover, the D- and E-bands are not even contiguous. Thus, while a war may take place on one, the E-band for instance, a bidder only interested in the D-band is penalized.

Issue #3: Triggering a 10% bid increment with just a single bid unfairly creates a permanent "edge effect" that always rewards "predatory or vengeance bidding" and lengthens the auction

a. **Background:** The minimum bid increment matrix calls for (at least) a 10% bid increment whenever a market has had a bid in either of the last two rounds. We presume this rule is motivated by the idea that prices of "contested" markets should rise faster than those of markets on which there is little bidding.

b. **The problem:** A problem the current minimum bid increment matrix creates, however, is to force the minimum bid increment to jump up to 10% as soon as **any** bid is placed, even if the market is clearly not active (e.g., even if it has gone many rounds without a bid). This circumstance unfairly rewards both "predatory or vengeance bidding" (i.e., where a bidder attacks a market on which it has previously shown no interest) and the "insincere" bidder (who bids on markets in which it is not interested during much of the auction). The rule simultaneously disadvantages bidders who show, in their bidding, consistent interest in a market. The unfairness is compounded at stage transitions, i.e., the parties will husband excess eligibility until the stage transition and then attack on the first round of the new stage solely because it is less expensive to attack than to defend. This benefit always accrues to those with the largest eligibility even if they plan on contracting later.

c. **An example:** Assume that it is fairly late in the auction (Stage 2 or 3), and some markets have gone many rounds without a bid. Bidder A has been high on such a market, and its minimum increment is 5%. Bidder B then bids on this market at a 5% increment. Bidder A is now faced with responding at a 10% increment. Thus, Bidder A, who has been sincerely bidding on a market

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of interest, is put at an unfair disadvantage compared to Bidder B, who has not been bidding this market. Bidder B thus has a higher chance of winning the market with a single bid, since Bidder A must respond with a bid that is two times higher at the margin than its competitor's. Further complicating Bidder A's situation is that, since it is late in the auction, the auction is now at multiple rounds per day, so that it has very little time to make this decision. Bidder A's dilemma is made worse by the fact that, according to the current minimum bid increment matrix, the market must have **no bids on it for the next two rounds before the increment returns to 5%** (this factor is discussed further in "Issue #4" below).

d. **Bidder A's alternatives:**

1. Rebid at the required minimum bid (15.5% higher than its own prior high bid).

2. Lose eligibility by not rebidding during the current round, even though it may be willing to rebid at a 5% increment.

    - Note that Bidder A may be willing to rebid at 5%, but the rules will not allow them to do so in this round (or, indeed, under the current "look-back" rule, in the subsequent round).

3. Bid on another market at a 5% increment, even though it has less interest in that market.

    - In other words, "park" on another market (or markets), thus putting another bidder into the same situation it finds itself in. Note the consequence of this: a **cascading effect, in which successively more bidders and more markets are drawn into the fray, destabilizing and lengthening (rather than shortening) the auction.**

4. Take two successive waivers until the bid increment returns to 5%.

- Note that this is not really a viable response, since bidders are limited to a total of 5 waivers during the auction, whereas they may be faced with this situation multiple times. Furthermore, this use of a waiver is not the purpose of waivers.

f. **The complex matrix lengthens the auction:** We presume that the FCC believes that any provision that increases the minimum bid increment (including the provision discussed in this situation) will speed up the auction. We disagree, and we feel that in this situation the temporary, artificially-higher bid increment imposed on defenders will almost certainly lengthen the auction. As noted above, the artificial incentive created for Bidder A to avoid loss of eligibility by bidding on a different market is likely to successively involve additional markets and draw more bidders into the renewed bidding. This situation would be significantly more serious than the scenario played out in the original C-Block auction.

The C-band auction had stabilized on the largest "core" markets by round 50, yet the auction continued to round 184. In that auction, bidding was extended more than one hundred rounds with only a small number of bidders and markets involved in any one round. Even without the added incentive given to the attacker we saw a domino effect in which two bidders vied for a market until finally one conceded that market and (rather than lose eligibility) bid on entirely new markets that had been inactive for many rounds. Since these new markets were typically smaller, the bidder was often forced to bid on more than one new market, thus multiplying the number of markets and bidders involved. In the DEF auction, the minimum bid rule will make the attacked bidder even more likely to switch to other markets (thus expanding the auction

activity) rather than simply defending the market (thus confining the auction activity). The overall effect, therefore, of the minimum bid matrix in which a single bid causes the bid increment to go from 5% to 10% is that the auction will be lengthened rather than shortened.

g. **A flawed premise:** Insofar as the matrix is applied to the situation we describe, we believe that the bid increment matrix is based on a flawed premise. The intent of the matrix appears to be that when a market has substantial activity, the minimum bid increment increases. The flawed premise, however, is that a single bid in a single round equates to "substantial activity." By this premise, a market that has received only a single bid in the past fifty rounds would be considered (if that sole bid were in either of the most recent two rounds) to have substantial bidding activity and be in need of having its activity accelerated by a higher minimum bid increment. **We disagree with that premise and feel that, as a minimum, a market receiving one bid in the current round and no bids in the prior round should not be considered to have substantial bidding activity and should not have its bid increment increased. (Similarly, of course, a market with no bids in the current round and one bid in the prior round should also not have its bid increment increased.)**

h. **Fairness:** Apart from the more detailed discussion, it also seems only fair that a bidder who had, for many rounds, been the high bidder on a market should have the opportunity to defend that market against a single "attacker" at the same minimum bid increment, rather than be penalized for consistency.

i. **Contrary to social value objectives:** The present rule as applied to this situation works contrary to the following auction objectives from a social value perspective:

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- Penalizes behavior of bidders who bid consistently on markets they are truly interested in.

- Rewards behavior of insincere bidders who deliberately drive up the prices of markets in which they have little interest.

- Makes it more difficult for a bidder to create a rational footprint that would support a viable business, since such a footprint is more easily disrupted and more difficult to defend.

- Penalizes bidders with specific ties to a local community or region, since they normally do not have an alternative of avoiding a loss of eligibility by bidding on other markets.

j. **Potential Solutions:** If the FCC declines to revise the matrix to specify 5% increments in all cases, we suggest that the FCC seriously consider either of the following alternative approaches to reduce the problem described above:

(1) **Alternative 1:** Revise the matrix such that the minimum bid increment remains at 5% when there is a single bid, going higher only if there are two or more bids on the market.

(2) **Alternative 2:** For a market receiving a single bid in the current round, allow the minimum bid increment to rise from 5% *only* if the market had *received at least one bid in the prior round.*

Either Alternative eliminates the reward for the aggressor and levels the playing field for the defender. Alternative 2, however, has the added advantage of accelerating the bidding when a market is being consistently bid on by two bidders (which, we presume, is the FCC's original intent in establishing the current rule). In other words, in the situation described above, Alternative 2 allows Bidder A (who had been the high bidder on a recently unbid market) to respond at 5% to a new attack by Bidder B, but then

the minimum bid increment would go to 10% for successive bids until one of
the two bidders does not respond.

Issue #4: The minimum bid increment matrix should allow the bid increment to return to the lowest level whenever a market has zero bids.

a.   **Background:** The current minimum bid increment matrix has the following provision when a market receives no bid in the current round, then the minimum bid increment is determined by the number of bids in the prior round. This rule keeps minimum bid increments at an elevated level for an additional round, even when there is no activity on that market.

b.   **Discussion:** We do not see any advantage to this particular "Look-Back" rule, and we believe that the minimum bid should return to the lowest level (i.e., 5% in Stages 2 and 3) once a market goes without a bid in a round. We further believe the current mechanism propagates behavioral distortions into the auction, compounding the complexity of bidders' calculations and projections without significantly improving the auction process. This rule also introduces anomalies, such as the following (assumes Stage 2 or 3), in which a market with less activity has a higher minimum bid increment:

	Round 32	Round 33
Market X		
Number of bids	3	2
Bid increment for next round		**10%**
Market Y		
Number of bids	3	0
Bid increment for next round		**15%**

c.   **Worsening of Issue #3:** This "Look-Back" rule worsens the problem discussed above under "Issue #3," in which, after many rounds of no bids, Bidder B places a bid on a market and Bidder A is forced to respond at a bid increment which is twice as high. Specifically. Bidder A must wait at least two rounds before it even has the opportunity to bid again on that market at a

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5% increment. Our proposed solution ("Alternative 2") to Issue #3 does introduce a "look-back" rule of a different kind, but in that case it is a delay in *increasing* the minimum bid increment rather than a delay in *decreasing* the increment. **Too low an increment is better than too high an increment, since a high increment can force a permanent, unrecoverable loss of eligibility, whereas too low an increment merely runs the risk of having the auction last just one additional round.**

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Issue #5: The asymmetric "edge effects" of graduated bidding increments invite "collusive" behavior or, at minimum, support "drafting" every other round.

The gradation of the bidding increments by level of bidding activity in its very nature provides an incentive to engage in "collusive" bidding whereby a bidder bids on markets where a "friendly" or geographically-complementary bidder bids concurrently. This behavior especially benefits those complementary bidders seeking to win both D and E licenses, since the "collusive" or supportive bids raise the bid increment to 15% for any bidders bidding against the complementary bidder, as long as it pursues both the D- and E-band. Like the unsportsmanlike running tactic where two runners box in an opposing runner to allow a third teammate to pass, the odd step functions built into the minimum bid increment matrix invites such tactics.

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Other comments

Waivers

The FCC should not look upon use of waivers as an appropriate solution to
bidders' problems with minimum bid increments, unless the FCC greatly expands
the number of available waivers (e.g., 50-100). Because of the limited number of
waivers available, they are clearly not a tool that can be used regularly during the
auction in situations that could arise any number of times. Rather, waivers must
be used for their originally intended purpose, namely, to provide a margin of
safety against equipment or communications problems or to allow the bidder to
deal with other unexpected internal problems.

Analysis Time

The DEF auction will have extraordinary complexity compared even to the C
Block auction. For example, the DEF auction will have three times the number of
licenses (1479 total); differing eligibility for the F block compared to the D and E;
some bidders filing for only certain blocks; different levels of bidding credits;
three levels of financing; and greater complexity of strategy interaction based on
the incumbents and technologies in other frequencies and neighboring markets. In
addition, the bid increment rules are vastly more complex than with any previous
auction, varying market by market in a complex way that is dependent on the
bidding pattern for the last two rounds. We hope that the FCC appreciates the
challenge that bidders will face simply in attempting to review the results of a
round. We believe that moving to multiple rounds per day early in the auction
would have a disastrous effect on the ability of bidders to make responsible
bidding decisions, and we urge the FCC to not to require multiple rounds per day
until the bidders have gained substantial experience and until the overall auction
activity level has diminished.

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Conclusion

We feel certain that the existing rules embodied in the minimum bid increment matrix and its supporting logic pose an array of unforeseen challenges and obstacles to both sophisticated and novice bidders alike. Again, we very much would support the FCC returning to its method of minimum bid calculation used in prior auctions, and would request the FCC, at a minimum, find equitable solutions to the issues we have raised.